PSD2 APPROACHES: AN OVERVIEW

Financial Services
PSD2 Approaches : an overview

Introduction and background

The recast Directive on Payment Services (or PSD2) is one of a series of legislative measures adopted by the European Union in response to rapid technological innovation and the desire to increase competition and integrate payment services across national borders. It must be implemented in the UK no later than 13 January 2018.

The current Payment Services Directive was adopted in 2007 and implemented in the UK through the Payment Services Regulations 2009. The Directive created a regulatory framework for payment services in the EU which aimed to create a well functioning, integrated and competitive single market, as well as providing the legal basis for the Single Euro Payments Area (SEPA).

The current regulations are no longer considered adequate; they have been applied inconsistently and EU policy makers believe they have not stimulated sufficient innovation and competition. At the same time, concerns have grown about the effectiveness of security measures associated with digital payments.

PSD2 seeks not only to reflect technological change, but to promote digital innovation (for example, by facilitating the market entry of new types of payment service providers). It also looks to provide greater transparency over charges, improve consumer protection and the security of payments.

We have set out below a summary of the key issues raised by PSD2. Over the next few months we will be issuing more detailed briefings on each of the key issues identified and exploring what these will mean in practice for firms.

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**PSD2 KEY ISSUES – AT A GLANCE**

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<tr>
<th>Geographical scope and currencies.</th>
<th>PSD2 extends the provisions relating to transparency and information requirements for</th>
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<td>► 2 leg in non-EU currency transactions</td>
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<th>Types of payment services and exemptions.</th>
<th>► Introduction of new payment services</th>
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<td>► Exemptions have been restricted and/or clarified for:</td>
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<td></td>
<td>► commercial agents,</td>
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<td>► limited networks,</td>
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<td>► telecoms,</td>
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<td>► ATM operators, and</td>
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<td>► the waiver regime - for “small” payment institutions.</td>
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<td>► The use of the limited network exemption will also impose an obligation on firms to report to the regulator where transactions utilising this exemption exceed EUR 1,000,000 within a 12 month period.</td>
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<tr>
<th>Access to payment accounts</th>
<th>► A customer will have the right to use a payment initiation service where their account is accessible online and their consent to the payment may be given via the payment initiation service.</th>
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<td>► Similarly, new account information services will afford</td>
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<td>PSD2 KEY ISSUES – AT A GLANCE</td>
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<td>consumers a consolidated view of their accounts, enabling access with a single online login.</td>
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<td>► Authorised payment institutions must be able to access payment accounts on an objective, non-discriminatory and proportionate basis. Where access is refused the customer must be informed (where possible) before denying access, and the regulator notified so that it can monitor the grounds of refusal.</td>
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Security of payments

► New frameworks to control and manage operational risks, including security risks relating to payments; payment services providers will need to have a security policy document, a description of their security incident management procedure and an explanation of their contingency procedures.

► New reporting requirements for major operational and security incidents.

► New obligations to notify customers of data breaches without undue delay where it may impact their financial interests.

► Strong customer authentication. – The validation of the identification of a person based on the use of two or more elements categorised as
  
  ► Knowledge – something only the user knows (PIN; password)
  
  ► Possession – something only the user has (CVV number; PINSentry code)
  
  ► Inherence – something only the user is (fingerprint; voice print)

This is to be used when accessing a payment account on-line, initiating "an electronic payment transaction or for any action, through a remote channel, which may imply a risk of payment fraud or other abuses.

► The European Banking Authority (EBA) will issue guidelines and regulatory technical standards to support the new requirements. However, timelines are problematic.

Liabilities & consumer protection

► Liability cap for unauthorised payment transactions reduced to 50 EUR. This will not impact payment service providers that do not apply this to customers.

► New rules on liability allocation as between the bank and payment initiation services. These rules will be mandatory, meaning that payment service providers cannot make the agreement of a different allocation of liability a condition of permitting access to their customers’ accounts.

► Payment service provider liability where strong customer authentication is not provided or accepted.

► Unconditional right to a refund for a SEPA direct debit. This is already available in some countries and in the UK through the direct debit guarantee scheme, but it will now be put on a legal basis.
### PSD2 KEY ISSUES – AT A GLANCE

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<th>Issue</th>
<th>Details</th>
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<td>Redress</td>
<td>► Out of court redress system – a full response within 15 business days.</td>
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<td>Non-discriminatory access to payment systems</td>
<td>► Access to payment systems to be objective, non-discriminatory and proportionate, and not to inhibit access to payment systems other than to safeguard settlement risk. Sponsor banks will need to review policies and agreements for compliance with the non-discrimination provisions.</td>
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Things to think about

Firms should start to assess how the proposed changes will affect them, for example:

► Consider the scope of your payment activities and the need to apply additional transparency and information requirements. Changes to framework agreements for payment accounts are likely to be required.

► Consider how to implement the increased security requirements. This will require a review of the security measures for accessing accounts and initiating payments. We recommend firms pay particular attention to the draft regulatory technical standards issued by the EBA and participate in the consultations to drive these changes forward in a direction that both meets the objectives of PSD2 and delivers good customer outcomes.

► Frameworks to control and manage operational risks, including security risks will need to be developed, where they do not exist already.

► Consider allocation of liability provisions within framework agreements and what changes need to be made.

► Review complaints processes and approaches to redress. This may also require firms to update customer facing literature.

► With the widened scope and narrowed exemptions firms will need to examine their business models. This may also impact third party supplier arrangements that can now be bought into scope.

Next steps

Over the next few months we will issue more detailed briefings on each of the key issues identified above. We will also look at the interplay between PSD2 and other legislative and regulatory developments. For example:

Interchange Fee Regulation

PSD2 is closely linked to the Interchange Fee Regulation for card based payment instruments. This is intended to introduce greater competition through new conduct of business rules and a cap on multilateral interchange fees or "MIFs." The key provision which came into force on 9 December 2015 caps the level of the interchange fee between acquirers and merchants that can be applied to a card transaction. New conduct of business rules include the prohibition on the "honour all cards rule," whereby card schemes or payment service providers require merchants to accept all cards of a certain brand. This and other measures, including separation of payment card schemes and processing, co-badging and unblending, will apply from 9 June 2016.

Payment Accounts Directive

The Payment Accounts Directive has been implemented in the UK by the Payment Account Regulations 2015. It seeks to improve the comparability of fees related to payment accounts, facilitate account switching and improve access to payment accounts with basic features. Payment service providers will have to provide consumers with a fee information document listing the most common payment services provided and the fees charged for each of them. Payment service providers must offer a switching service for Payment Accounts that are denominated in the same currency and provide assistance to any consumer who wants to open an account in another EU Member State. There must be non-discriminatory access to payment accounts in the UK so that consumers legally resident in the EU have the right to open and use such a payment account, irrespective of their place of residence. Moreover, nine payment service providers have currently been required to offer a payment account with basic features to consumers. A basic bank account must be provided either free of charge or for a reasonable fee.
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